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11 September 1985

SOVIET OIL PROBLEMS

In a televised speech delivered at the end of his visit to West Siberia last week, Gorbachev lashed out at Soviet geologists, implying that they misled the leadership into believing that there were no problems with expecting continuing increases in oil output from West Siberia, which supplies 60 percent of Soviet oil.

- He promised further major increased in investment in the area but said that in terms of prospects "we had the rise, the peak, and now we have the decline," apparently laying the groundwork for reduced goals for future output.
- Indeed, month-to-month-decreases in Soviet oil output have averaged 4% or nearly 500,000 b/d through the first half of 1985 as compared with 1984 and Gorbachev's lengthy visit to West Siberia indicates this rate of decline likely continued in July and August.

The fall in oil production will prove a major test for Gorbachev's economic and political leadership.

- The problems in West Siberia go far beyond geology; many potentially productive wells are out of service due to a lack of equipment.
- In essence, the difficulties go to the core of the economic system with its competing priorities and unfulfilled plans.
- While some outside analysts point to the out-of-service wells as a reason for the Soviets to be optimistic about turning around the production decline, the inability of the Soviet system to respond to this problem many months after it was recognized demonstrates the magnitude of the difficulties.

Owing to the failure of the Soviet system to conserve energy and replace domestic oil with gas, the Soviets now face the prospect of a rapid decline in hard currency earnings as shipments to Western Europe are cut back.

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- Press reports in Europe confirm the Petroleum Intelligence Weekly story that many customers will be cut back from 30 to 50 percent, representing a loss of perhaps \$3 to 4 billion in annual oil revenues or more than 10 percent of total hard currency earnings.
- The magnitude of this decline means that the reduction in Soviet earning power between now and 1990 which CIA recently forecast is proceeding more rapidly than even the "worst case" estimates.

Moscow recently began pushing the countries in Eastern Europe to increase their participation in gas development.

- If the Soviets also go back to these countries and ask them to take further reductions in oil deliveries, this will put even more pressure on their political relationships.
- These countries were hurt badly by the oil reductions that took place earlier this year and can be expected to lobby hard against taking any further cuts.

In any case, the Soviet-East European economic relationship seems headed for more trouble.

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